

Message Text

CONFIDENTIAL

PAGE 01 ROME 00569 01 OF 05 140940Z
ACTION EUR-08

INFO OCT-01 SS-14 ISO-00 FRB-01 NSC-05 NSCE-00 INR-05
CIAE-00 INRE-00 SP-02 L-01 EB-03 OMB-01 SSO-00 /041 W
-----140952Z 039880 /12

O R 140822Z JAN 77
FM AMEMBASSY ROME
TO SECSTATE WASHDC IMMEDIATE 2154
TREAS DEPT WASHDC IMMEDIATE
INFO USMISSION EC BRUSSELS
USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 1 OF 5 ROME 0569

LIMDIS

PASS FRB

E.O. 11652: GDS
TAGS: EFIN, IT
SUBJ: CURRENT STATUS OF ECONOMIC STABILIZATION PROGRAM

REF: (A) 76 ROME A-514, (B) 76 ROME 20147, (C) 76 ROME 19891,
(D) 76 ROME 19449, (E) 76 ROME 18880

1. SUMMARY. FOLLOWING REPORT IS DESIGNED TO GIVE CURRENT
EMBASSY ASSESSMENT OF GOI ECONOMIC STABILIZATION EFFORTS.
ASSESSMENT IS OBVIOUSLY PRELIMINARY, SINCE FINAL COMPONENTS
OF PROGRAM, PARTICULARLY IN LABOR COST AREA BUT ALSO IN
FISCAL AREA, HAVE NOT YET BEEN DECIDED UPON BY GOI. BASIC
CONCLUSIONS ARE: FIRST, FISCAL EFFORT TO DATE IS COMMENDABLE
BUT DOUBTS REMAIN ABOUT POTENTIAL 1977 CASH EXPENDITURES FOR
WHICH FINANCING IS NOT YET AVAILABLE. POTENTIAL EXCESS
EXPENDITURES WHICH MAY BE REALLY DIFFICULT TO DEFER ARE
PROBABLY IN RANGE 2,000 TO 3,000 BILLION LIRE. GOI WILL
CERTAINLY GO AHEAD WITH SOME ADDITIONAL TAX MEASURES, AT
LEAST TO FINANCE SOME FISCALIZATION OF SOCIAL COSTS AND
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 00569 01 OF 05 140940Z

PROBABLY SOME EXCESS EXPENDITURES. SECOND, GOI HAS
RECENTLY TAKEN FAIRLY STRONG STANCE ON NEED TO MODIFY
WAGE ADJUSTMENT MECHANISM (SCALA MOBILE) BUT HAS
ENCOUNTERED STRONG LABOR OPPOSITION. NONETHELESS, THERE
IS STILL FAIRLY GOOD PROSPECT THAT SCALA MOBILE ITSELF
CAN BE REVISED IN SOME WAY TO SUPPLEMENT OTHER LABOR
COST REDUCTION (I.E., PARTIAL BLOCK OF SCALA MOBILE LIMITATIONS ON COM

PANY LEVEL WAGE RATE

INCREASES AND FISCALIZATION OF SOCIAL COSTS). TOTAL LABOR COST PACKAGE COULD APPROACH 4,000 BILLION LIRE OR ABOUT 4 TO 5 PERCENT OF POTENTIAL 1977 LABOR COSTS. THIRD, GOI PERFORMANCE IN MONETARY FIELD (E.G., DOMESTIC CREDIT EXPANSION AND CENTRAL BANK FINANCING OF TREASURY DEFICIT) HAS BEEN GIVEN RELATIVELY LITTLE ATTENTION BY IMF RECENTLY BECAUSE OF CONCENTRATION OF FISCAL AND LABOR COST PROBLEMS. PROVIDED GOI CAN HOLD THE LINE ON TREASURY DEFICIT, WE DO NOT EXPECT GREAT DIFFICULTY FOR GOI IN REACHING AGREEMENT ON MONETARY CEILINGS. FOURTH, MUCH-DEBATED QUESTION OF ZERO GROWTH AND POSSIBLE RISING UNEMPLOYMENT IN 1977 NEEDS TO BE PUT IN PROPER PERSPECTIVE. IN 1976 REAL GROWTH WAS AT A RECORD LEVEL (EXCEEDING PREVIOUS 1974 RECORD GDP). THUS, STAGNATION OR EVEN SOME SMALL DECLINE IN GDP IN 1977 WOULD STILL MEAN THAT ABSOLUTE LEVEL OF ECONOMIC ACTIVITY WOULD REMAIN AT VERY HIGH LEVEL. RECENT ASSERTION BY MINISTER OF INDUSTRY DONAT-CATTIN THAT UNEMPLOYMENT COULD RISE BY 600 THOUSAND IS NOT CREDIBLE. EVEN FIGURE OF 200-300 THOUSAND MENTIONED BY MINISTER OF LABOR ANSELMI MAY BE ON HIGH SIDE. END SUMMARY.

2. TREASURY DEFICIT. TABLE 1 BELOW SHOWS SUMMARY DATA ON TREASURY CASH DEFICIT FOR PERIOD 1974-1977. ESTIMATES FOR 1976 AND 1977 ARE FROM GOI SOURCES. ONLY CHANGE IN 1977 ESTIMATES IN TABLE 1 FROM THAT REPORTED REFS A AND B IS INCREASE IN ASSUMED CONSOLIDATION OF LOCAL GOVERNMENT DEBTS FROM 5,500 BILLION TO 6,000 BILLION LIRE.HNOTE THAT

CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 00569 01 OF 05 140940Z

THIS CHANGE DOES NOT AFFECT EITHER NET TREASURY DEFICIT OR CREDIT TO TREASURY, SINCE IMF AND EC EXCLUDE DEBT CONSOLIDATION FROM CEILINGS ON CREDIT TO TREASURY. IF GOI SUCCEEDS IN HOLDING NET TREASURY CASH DEFICIT IN 1977 TO 10,100 BILLION LIRE, THEN RATIO OF CASH DEFICIT TO GDP WOULD FALL SUBSTANTIALLY, I.E., TO ABOUT 6 PERCENT. THIS WOULD BE LOWEST RATIO ACHIEVED SINCE 1970 AND BE ONLY SLIGHTLY HIGHER THAN 1965-1970 ERIOD (AVERAGE 4.2 PERCENT) WHEN BUDGET DEFICIT HWAS NOT A SERIOUS PROBLEM.

3. TABLE 1 - TREASURY CASH DEFICIT 1974-1977 (BILLIONS OF LIRE)

	1974	1975	1976E	1977E
CENTRAL GOVERNMENT	-5,204	-10,213	-10,450	-11,000
NON-BUDGET	-3,758	-6,351	-4,550	-6,500
GROSS DEFICIT	-8,962	-16,564	-15,000	-17,500
LESS: DEBT CONSOL.	315	2,393	400	7,400
NET DEFICIT	-8,647	-14,171	-14,600	-10,100
(AS PERCENT GDP)	(8.7)	(12.6)	(10.6)	(6.1)

LESS: TREAS. CONTR.

TO SP. CR. INST. 127 522 800 300

CREDIT TO TREASURY -8,520 -13,649 -13,800 -9,800

ACTUAL ELEVEN MONTHS: 12,658 BILLION LIRE

E - ESTIMATE

4. TABLE 2 SHOWS DATA FOR 1974-1977 ON CENTRAL GOVERNMENT TAX RECEIPTS (CASH BASIS), WITH ANNUAL PERCENT CHANGES BOTH IN NOMINAL AND IN REAL TERMS. ESTIMATE FOR CALENDAR 1976 MAY BE SOMEWHAT ON HIGH SIDE SINCE TAX INCREASE DURING FIRST NINE MONTHS OF YEAR WAS ONLY 26 PERCENT ABOVE SAME PERIOD OF 1975, WHILE GOI ESTIMATE FOR ENTIRE YEAR IS FOR INCREASE OF 34HPERCENT. HOWEVER, SOME OF TAX PACKAGE WILL SHOW UP IN FOURTH QUARTER (GASOLINE, ADVANCE PAYMENT OF ONE-THIRD OF BANK INTEREST WITHHOLDINGS AND FOREIGN EXCHANGE TAX) AND COULD BOOST REVENUES UP TO GOI FORECAST. ON OTHER HAND, FORECAST TAX RECEIPTS FOR 1977,

CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 00569 01 OF 05 140940Z

IF ANYTHING, MAY BE UNDERESTIMATED. (AFTER NETTING OUT EFFECT OF RECENT TAX MEASURES, UNDERLYING GROWTH OF REVENUES SHOWS NOMINAL INCREASE OF 22 PERCENT BUT REAL INCREASE OF LESS THAN 1 PERCENT.) IN SUM, GOI ESTIMATES OF REVENUE SIDE FOR 1977 DO NOT APPEAR UNREALISTIC. INDEED, FINANCE MINISTER PANDOLFI HAS REPEATEDLY INSISTED THAT REVENUE ESTIMATES ARE TOO LOW.

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 00569 02 OF 05 141021Z

ACTION EUR-08

INFO OCT-01 SS-14 ISO-00 FRB-01 NSC-05 NSCE-00 INR-05
CIAE-00 INRE-00 SP-02 L-01 EB-03 OMB-01 SSO-00 /041 W
-----141028Z 040236/21

O R 140822Z JAN 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 2155

TREAS DEPT WASHDC IMMEDIATE

INFO USMISSION EC BRUSSELS

USMISSION OECD PARIS

CONFIDENTIAL SECTION 2 OF 5 ROME 0569

LIMDIS

PASS FRB

5. TABLE 2 - CENTRAL GOVERNMENT CASH TAX RECEIPTS, 1974-1977
(PERCENT CHANGE; BILLIONS OF LIRE)

	1974	1975	1976E	1977E#	1977E##
TOTAL TAXES	17,711	19,751	26,500	35,750	32,306

PERCENT CHANGE:

NOMINAL	30.0	11.5	34.2	34.9	21.9
---------	------	------	------	------	------

REAL	11.3	-5.2	15.2	11.7	0.9
------	------	------	------	------	-----

(GDP DEFULATOR)	16.8	17.5	16.5	20.9	20.9
-----------------	------	------	------	------	------

WITH NEW TAXES

WITHOUT NEW TAXES

E - ESTIMATE. (ACTUAL NINE MONTHS 1976: NOMINAL 26.4

PERCENT, REAL 6.4 PZRCENT)

6. TABLE 3 SHOW CENTRAL GOVERNMENT CASH EXPENDITURES
FOR PERIOD 1974-1977 AND ANNUAL PERCENT CHANGES IN NOMINAL
AND REAL TERMS. GOI ESTIMATE OF EXPENDITURES INCREASE FOR
CALENDAR 1976 APPEAR SOMEWHAT ON LOW SIDE AT 32 PERCENT, COM-
PARED TO 43 PERCENT IN FIRST NINE MONTHS. ALSO, ESTIMATED 24
PERCENT INCREASE IN EXPENDITURES FOR 1977 APPEARS
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 00569 02 OF 05 141021Z

SOMEWHAT LOW IN VIEW OF EXPECTED RATE OF INFLATION THAT
YEAR. (POSSIBLE OVERESTIMATION OF CENTRAL GOVERNMENT
TAXES IN 1976 AND POSSIBLE UNDERESTIMATION OF EXPENDITURES
RAISE SOME DOUBTS ABOUT CREDIBILITY OF GOI INSISTENCE
THAT IT WILL RESPECT LAST YEAR'S LIMIT ON CASH BUDGET
DEFICIT. ON OTHER HAND, TOTAL TUREASURY CASH OPERATIONS
THROUGH FIRST ELEVEN MONTHS SHOW DEFICIT OF 12,658
BILLION LIRE, WHICH IS ABOUT ON TARGET.) FOR 1977 THIS
RELATIVELY LOW PROJECTED GROWTH RATE FOR EXPENDITURES
RAISES QUESTIONS ABOUT GOI ACHIEVEMENT OF PROPOSED CASH
BUDGET TARGET. HOWEVER, POSSIBILITY THAT REVENUE
ESTIMATES ARE ALSO TOO LOW WOULD TEND TO OFFSET ANY
EXCESS OF EXPENDITURES.

7. TABLE 3 - CENTRAL GOVERNMENT CASH EXPENDITURES IN REAL
TERMS, 1974-1977 (PERCENT CHANGE; BILLIONS OF LIRE)

	1974	1975	1976E	1977E
TOTAL EXPENDITURES	25,827	32,424	42,950	53,150

PERCENT CHANGE:

NOMINAL	17.3	25.5	32.5	23.7
---------	------	------	------	------

REAL	0.4	6.7	13.7	2.4
------	-----	-----	------	-----

(GDP DEFULATOR)	16.8	17.5	16.5	20.9
-----------------	------	------	------	------

E - ESTIMATE. (ACTUAL NINE MONTHS 1976: NOMIANL 42.6

PERCZNT; REAL 20.0 PERCENT.)

8. TABLE 4 SHOWS SOME DATA PUBLISHED IN TURIN'S "LA STAMPA" JANUARY 12 ON SUPPOSED CASH EXPENDITURES IN 1977 EXPENDITURES FOR WHICH FINANCING IS NOT AVAILABLE. (SEE REFS B AND C.) DATA IN TABLE 4 SHOULD BE EXAMINED WITH GREAT CARE SINCE IT IS CLEAR THAT, FOR TACTICAL REASONS, TREASURY MINISTER STAMMATI IS USING SUCH FORECASTS IN EFFORT TO PERSUADE PUBLIC AND PARLIAMENT OF SERIOUSNESS OF TREASURY DEFICIT PROBLEM AND POSSIBLE NEED FOR SOME ADDITIONAL TAXES. NOTE, FOR EXAMPLE, THAT: (1) ACCORDING TO BOI SOURCE, PART OF WAGE CONTRACT COST IS ALREADY PROVIDED FOR IN CENTRAL GOVERNMENT CASH BUDGET ESTIMATES

CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 00569 02 OF 05 141021Z

FOR 1977 (250 BILLION LIRE) AND THAT TREASURY WILL NOT NECESSARILY BECOME RESPONSIBLE FOR FINANCING WAGE COSTS OF OTHER PARTS OF PUBLIC ADMINISTRATION. (2) CONSOLIDATION OF PAST DEBTS OF HOSPITAL AND HEALTH INSURANCE FUNDS IS NOT ABSOLUTELY NECESSARY SINCE FINANCING HAS ALREADY BEEN PROVIDED IN SOME FORM, ALTHOUGH PROBABLY SHORT-TERM AND AT HIGH INTEREST. (WE HAVE ASSUMED, ON BASIS DISCUSSION WITH BOI, THAT 1,400 BILLION LIRE IN DEBT CONSOLIDATION OF HOSPITALS AND HEALTH INSURANCE FUNDS WILL TAKE PLACE IN 1977, AND THIS FIGURE IS CONTAINED IN CASH DEFICIT ESTIMATES IN TABLE 1 ABOVE.) IN ANY CASE, FINANCING OF DEBT CONSOLIDATION IS EXCLUDED FROM IMF AND EC CEILINGS. (3) FINANCING OF NEW DEFICITS IN 1977 OF HOSPITALS AND HEALTH INSURANCE FUNDS CANNOT BE AVOIDED BUT BOI SOURCE HAS INDICATED THAT FINANCING OF HEALTH INSURANCE DEFICIT SEEMS TO BE ADEQUATELY PROVIDED FOR WITHOUT NEED TO CALL UPON TREASURY. SAME BOI SOURCE SUGESTED THAT UNCOVERED PART OF 1977 HOSPITAL DIFCITS MIGHT BY ONLY 900 BILLION LIRE RATHER THAN 1,900 BILLION LIRE. (4) ON OTHER HAND, IN ADDITION OTO ITEMS SHOWN IN TABLE 4, THERE HAS BEEN DEBATE ABOUT WHETHER ADDITIONAL FUNDS WILL BE NEEDED FOR OTHER PURPOSES SUCH AS FRIULI RECONSTRUCTION, ENDOWMENT FUNDS OF STATE HOLDING COMPANIES INCLUDING EGAM, HEALTH REFORM AND NEW PROGRAMS FOR INDUSTRIAL RECONVERSION, AGRICULTURE, YOUTH EMPLOYMENT AND HOUSING. EMBASSY ANALYSIS OF TABLE 4 AND OF OTHER ITEMS NOT INCLUDED THEREIN SUGGEST THAT UNDEFERRABLE, UNCOVERED EXPENDITURES COULD BE IN RANGE 2,000 TO 2,500 BILLION LIRE.

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 00569 03 OF 05 141056Z

ACTION EUR-08

INFO OCT-01 SS-14 ISO-00 FRB-01 NSC-05 NSCE-00 INR-05
CIAE-00 INRE-00 SP-02 L-01 EB-03 OMB-01 SSO-00 /041 W
-----141100Z 040618/21

O R 140822Z JAN 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 2156

TREASURY DEPT WASHDC IMMEDIATE

INFO USMISSION EC BRUSSELS

USMISSION OECD PARIS

C O N F I D E N T I A L SECTION 3 OF 5 ROME 0569

LIMDIS

PASS FRB

9. TABLE 4 - POSSIBLE EXCESS EXPENDITURES IN 1977

(BILLIONS OF LIRE)

WAGE CONTRACT IN PUBLIC ADMINISTRATION 900

DEBT CONSOLIDATION: 3,510

HOSPITALS 75-76 1,650

HEELTH INSURANCE 75-76 1,860

DEFICIT FINANCING: 3,040

HOSPITALS 1977 1,900

HEALTH INSURANCE 1977 1,140

OTHER: 40

NEWSPAPER SUBSIDY 30

ROME SUBWAY 10

TOTAL 7,490

10. PROSPECTS FOR INTRODUCING NEW SUPPLEMENTARY TAX

PACKAGE TO COVER POSSIBLE EXCESS EXPENDITURES IN 1977

AND ALSO TO FINANCE ANY FISCALIZATION OF SOCIAL COSTS

WHICH MAY BE INCLUDED IN FINAL LABOR COST PACKAGE ARE

STILL HIGHLY UNCERTAIN. TREASURY MINISTER STAMMATI

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 00569 03 OF 05 141056Z

CONTINUES TO TAKE VERY HARD LINE IN DEFENSE OF PROPOSED
9,800 BILLION LIRE CEILING ON CREDIT TO TREASURY IN 1977,
ARGUING THAT IF ADDITIONAL EXPENDITURES MUST BE MADE,
THEN, CONSTITUTIONALLY, HE IS OBLIGED TO ASSURE THAT
FINANCING IS PROVIDED. FINANCE MINISTER PANDOLFI, IN
CONTRAST, CONTINUES TO RESIST IDEE OF ADDITIONAL TAXES,

PARTICULARLY INCREASES IN PERSONAL INCOME TAX RATES. HE RECENTLY CLAIMED THAT IMPROVED TAX COLLECTIONS IN 1977 COULD GENERATE 2,000 BILLION LIRE IN REVENUES ADDITIONAL TO THAT CONTAINED IN PRESENT CASH BUDGET FORECASTS. HOWEVER, HE HAS ALSO ACKNOWLEDGED THAT IF LARGE PART OF POSSIBLE EXCESS EXPENDITURES ARE IN FACT MADE, IMPROVED TAX COLLECTIONS ALONE WOULD NOT SUFFICE. PRIME MINISTER ANDREOTTI IN RECENT TV INTERVIEW SEEMED TO COME DOWN ON STAMMATI'S SIDE OF ARGUMENT. IN ANY CASE, IT IS AGREED AMONG ALL THREE PARTIES TO LABOR COST NEGOTIATIONS THAT ANY FISCALIZATION MEASURE MUST BE ACCCOMPANIED BY ADDITIONAL TAXES TO COVER COST TO TREASURY. SOME INCREASE IN VALUE ADDED TAX IS MOST LIKELY PROSPECT, ALTHOUGH LABOR UNIONS ARE PUSHING FOR INCREASED INCOME TAX RATE ON UPPER INCOMES. RECENT ESTIMATES OF REVENUE WHICH COULD BE GENERATED BY UNIFICATION UPWARD OF EXISTING VALUE ADDED (IVA) TAX RATES INTO FOUR CATEGORIES SHOWED FIGURE OF 3,200 BILLION LIRE (REF D). HOWEVER, IT SEEMS UNLIKELY THAT IVA INCREASE OF THIS SIZE WOULD BE ADOPTED IN LARGE PART BECAUSE OF INFLATIONARY FEED-BACK EFFECT THROUGH SCALA MOBILE. (POSSIBILITY OF EXCLUDING EFFECT ON SCALA MOBILE OF IVA TAX RATE CHANGES DOES NOT LOOK PROMISING.) PARTLY TO PLEASE LABOR UNIONS AND PARTLY TO SUPPLEMENT POSSIBLE IVA TAX INCREASE, GOI MAY EVENTUALLY AGREE TO SOME FORM OF PERSONAL INCOME TAX INCREASE.

11. IN EMBASSY VIEW, TOTAL NEW REVNU PACKAGE, WHATEVER ITS COMPOS TION, IS NOT LIKELY TO BE LARGER THAN ABOUT 2,500 BILLION LIRE. IMPLICITLY, THIS MEANS THAT IF FISCALIZATION COSTS 1,100 BILLION LIRE ONLY 1,400 BILLION

CONFIDENTIAL

CONFIDENTIAL

PAGE 03 ROME 00569 03 OF 05 141056Z

LIRE (SEE PARA 13) WOULD REMAIN AVAILABLE TO FINANCE EXCESS EXPENDITURES. THUS, EVEN IF EXCESS EXPENDITURES COULD BE CONTAINED WITHIN RANGE 2,000 TO 2,500 BILLION LIRE, PROPOSED 9,800 BILLION LIRE FORECAST ON CREDIT TO TREASURH COULD BE PUSHED UP IN RANGE 10,400 TO 10,900 BILLION LIRE UNLESS REVENUE FORECASTS ARE TOO LOW, AS PANDOLFI CLAIMS. WHILE THESE ESTIMTES RE OBVIOUSLY "SOFT," IF CREDIT TO TREASURY SHOULD REACH UPPER LIMIT THIS COULD HAVE WORRISOME EFFECTS ON EXPANSION OF MONETARY BASE AND ON INFLATIVM

12. LABOR COSTS. FINAL OUTCOME OF NEGOTIATIONS AMONG GOVERNMENT, UNIONS AND MANAGEMENT ON LABOR COST QUESTION IS ST LL HIGHLY UNCERTAIN. WHILE APPARENTLY INTRANSIGENT POSITION ADOPTED BY THREE CONFEDERATIONS AT JANUARY 7-8 NATIONAL ASSEMBLY MAY BE PARTLY PUBLIC POSTURING, IT WILL NOT BE EASY TO REACH AGREEMENT ON ANY MEASURE WHICH DIRECTLY LIMITS FULL APPLICATION OF SCALA MOBILE. GOI/ BOI WORKING GROUPS HAVE BEEN T DYING WIDE VARIETY OF

OLD AND NEW PROPOSALS. CHANGE IN FREQUENCY OF ADJUSTMENTS FROM QUARTERLY TO SEMIANNUAL NOW APPEARS TO BE A NON-STARTER GIVEN STRONG LABOR UNION OPPOSITION. COMPROMISE FORMULA WILL PRESUMABLY BUILD UPON IDEAS ACCEPTABLE TO UNIONS. THIS MIGHT INCLUDE MODEST CHANGE IN SCALA MOBILE BASKET, POSSIBLY TO EXCLUDE OR REDUCE WEIGHTS OF URBAN TRANSPORT, NEWSPAPERS AND MAYBE SOME PUBLIC UTILITY RATES. SOME FORM OF CAP ON MAXIMUM AMOUNT OF ADJUSTMENT WHICH CAN TAKE PLACE IN ANY GIVEN QUARTER HAS BEEN FAVORABLY MENTIONED BY ONE PCI SPOKESMAN. GOI MAY ALSO WISH TO NAIL DOWN SPECIFIC UNION COMMITMENTS TO REMOVE "ANOMALIES" BY UNIFYING SCALA MOBILE SYSTEM THROUGHOUT ALL ECONOMIC SECTORS (I.E., ELIMINATING PRIVILEGED TREATMENT NOW GIVEN TO BANK, INSURANCE, CHEMICAL AND SOME OTHER WORKERS). SIMILARLY, UNION PROPOSAL FOR UNLINKING SCALA MOBILE FROM SEVERANCE AND SENIORITY PAY MAY BE ADOPTED, EVEN THOUGH VALUE OF THIS PROPOSAL APPEARS QUITE LIMITED.

CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 00569 03 OF 05 141056Z

13. IN ADDITION TO WHATEVR COMPROMISE MAY BE REACHED ON MEASURES TO DIRECTLY AFFECT SCALA MOBILE MECHANISM, EMBASSY ASSUMES THAT OVERALL LABOR COST PACKAGE WILL ALSO INCLUDE SOME ESTIMATE FOR REDUCED WAGE RATE INCREASES DUE IN IMPENDING COMPANY-LEVEL NEGOTIATIONS AND SOME FISCALIZATION OF SOCIAL COSTS BORNE BY BUSINESS. AT JANUARY 7-8 MEETING, UNION LEADERS, IN STRONGLY DEFENDING "UNTOUCHABILITY" OF SCALA MOBILE, TRIED TO PERSUADE MEETING PARTICIPANTS THAT QUID PRO QUO FOR DEFENDING SCALA MOBILE WOULD HAVE TO BE RESTRICTIONS ON COMPANY LEVEL WAGE INCREASES. EMBASSY DOUBTS THAT UNIONS WILL BE VERY SUCCESSFUL AT THIS, BUT BELIEVES THAT PUBLIC POSTURE WILL NOW FORCE LEADERSHIP TO MAKE SERIOUS EFFORT. ON FISCALIZATION, ALL THEE PARTIES TO NEGOTIATIONS AGREE THAT SOMETHING SHOULD BE DONE, WITH GOI APPARENTLY KEEPING THIS INSTRUMNT IN RESERVE UNTIL OUTCOME OF CALA MOBILE TALKS HAVE BEEN CONNLUDED. PUBLIC POSITIONS ON AMOUNT OF FISCALIZATION ARE : (1) GOI 500 TO 700 BILLION LIRE, (2) CONFININDUSTRIA 3,500 BILLION LIRE, AND (3) PSI AND PCI 1,500 AND 1,000 BILLION LIRE, RESPECT VELY. HIGH LEVEL TREASURY MINISTRY OFFICIAL SUGGESTED TO EMBOFFS THAT COMPROMISE FIGURE OF AROUND 1,100 TO 1,200 BILLION LIRE MIGHT EVENTUALLY BE AGREED TO. AMOUNT OF FISCALIZATION WILL ALSO DEPEND UPON SIZE OF ADDITIONAL TAX PACKAGE WHICH CAN BE AGREED UPON, AS DISCUSSED ABOVE.

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 00569 04 OF 05 140914Z

ACTION EUR-08

INFO OCT-01 SS-14 ISO-00 FRB-01 NSC-05 NSCE-00 INR-05
CIAE-00 INRE-00 SP-02 L-01 EB-03 OMB-01 SSO-00 /041 W
-----140953Z 039704 /12

O R 140822Z JAN 77

FM AMEMBASSY ROME

TO SECSTATE WASHDC IMMEDIATE 2157

TREASURY DEPT WASHDC IMMEDIATE

INFO USMISSION EC BRUSSELS

USMISSION OECD PARIS

CONFIDENTIAL SECTION 4 OF 5 ROME 0569

LIMDIS

PASS FRB

14. TABLE 5 SHOWS EMBASSY CURRENT ROUGH ESTIMATE OF WHAT FINAL LABOR COST PACKAGE MIGHT LOOK LIKE. ITEM CONCERNING REVISIONS OF SCALA MOBILE CONSISTS OF PRESUMED TOTAL EFFECT OF VARIOUS INDIVIDUAL MEASURES WHICH MIGHT INCLUDE ELIMINATING ANOMALIES, SLIGHTLY REVISING SCALA MOBILE BASKET AND SOME LIMITATION ON NUMBER OF ADJUSTMENT POINTS APPLIED.

15. TABLE 5 - POSSIBLE LABOR COST HACKAGE (PERCENT OF LABOR COST; BILLIONS OF LIRE)

PERCENT 1) AMOUNT		
PARTIAL BLOCK ON HIGH INCOMES	0.6	600
LIMIT COMPANY LEVEL WAGE INCREASES	1.0	950
REVISIONS OF SCALA MOBILE	1.6	1,500
FISCALIZATION OF SOCIAL COSTS	1.2	1,100
TOTAL	4.4	4,150 2)

1) CALCULATED ON ESTIMATED TOTAL DEPENDENT LABOR COSTS
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 00569 04 OF 05 140914Z

OF 95,400 BILLION LIRE IN 1977, AN INCREASE OF 20 PERCENT OVER 1976.

2) TO PUT IT ANOTHER WAY, ANTICIPATED GROWTH OF LABOR

COSTS WOULD BE REDUCED FROM A 20 PERCENT RATE OF INCREASE
TO UNDER 15 PERCENT.

16. NET TRANSFER OF RESOURCES. TABLE 6 REPRESENTS VERY ROUGH ATTEMPT TO SUM UP NET TRANSFERS OF RESOURCES AMONG THREE SECTORS--HOUSEHOLD, BUSINESS AND PUBLIC ADMINISTRATION--OF: (1) EXISTING REVENUE PACKAGE (SEE REF E), AND (2) POSSIBLE ADDITIONAL FISCAL AND LABOR COST MEASURES. NEW FISCAL PACKAGE WOULD RESULT IN NO NET INCREASE IN TRANSFER OF RESOURCES TO PUBLIC ADMINISTRATION SINCE IT WOULD BE USED TO FINANCE FISCALIZATION AND TO COVER PRESUMED ADDITIONAL EXPENDITURES. (BENEFIT TO GOVERNMENT, AS EMPLOYER, OF LABOR COST REDUCTIONS, IS IGNORED.) DATA TEND TO OVERSTATE NET EFFECT OF RESOURCES TRANSFERRED FROM HOUSEHOLDS SINCE NO PROVISION IS MADE FOR UPWARD WAGE ADJUSTMENTS DUE TO FEED-BACK EFFECT OF SUPPOSED NEW IVA TAX INCREASE WORKING THROUGH SCALA MOBILE. WITH REGARD TO PARTIAL BLOCK OF SCALA MOBILE, QUESTION OF TIMING OF RE-TRANSFER TO BUSINESS OF PROCEEDS FROM SPECIAL TREASURY SECURITIES IS IGNORED. FINALLY, EXTENT TO WHICH NET TRANSFER OF RESOURCES TO BUSINESS SECTOR WOULD RESULT IN NEW INVESTMENT IN 1977 IS UNCERTAIN, SINCE RESOURCES MIGHT BE USED FOR SOME OTHER PURPOSE OR INVESTMENT MIGHT BE DELAYED BEYOND 1977.

17. TABLE 6 - NET TRANSFER OF RESOURCES (BILLIONS OF LIRE)

	HOUSE-	PUBLIC	
	HOLDS	BUS.	ADMIN.
EXISTING REVNURE PACKAGE	-3,644	-1,106	4,750
NEW F SCAL PACKAGE: 1)	-1,890	-610	2,500
EXCESS EXPENDITURES 2)	490	910	-1,400

CONFIDENTIAL

PAGE 03 ROME 00569 04 OF 05 140914Z

FISCALIZATION	-	1,100	-1,100
OTHER LABOR COST MEASURES:			
PARTIAL BLOCK	-600	600	-
COMPANH WAGE NEGOTIATIONS	-950	950	-
SCALA MOBILE REVISIONS	-1,500	1,500	-
TOTAL	-8,094	3,344	4,750

1) ASSUME: HOUSE- PUBLIC
HOLDS BUS. ADMIN.
IVA AQNQRP -610 1,750
INCOME TAX -750 - 750
TOTAL -1,890 -610 2,500

2) ASSUMES 65:35 SHARE BETWEEN BUSINESS AND HOUSEHOLDS.

18. GROWTH AND EMPLOYMENT. QUESTION OF "ZERO" GROWTH IN

1977 HAS BECOME MATTER FOR LIVELY DEBATE BOTH IN ECONOMIC AND POLITICAL TERMS. INITIALLY, TREASURY MINISTER STAMMATI SEEMED TO BE VIEWING ZERO GROWTH AS "TARGET" FOR 1977 AND WAS STRONGLY CRITICIZED FOR THIS. RECENTLY, GOI HAS BEEN MORE SUCCESSFUL IN PERSUADING PUBLIC AND LOOR UN ONS THAT, UNLESS GOOD STABILIZATION PROGRAM IS INTRODUCED WHICH WOULD ENCOURAGE EXPORTS AND INVESTMENT, ZERO GROWTH WILL BE RESULT OF SUCHH AN INADEQUATE STABILIZATION PROGRAM.

19. EVEN IF ZERO GROTH SHOULD OCCUR IN 1977, AND ASSUMING THAT REAL GROWTH IN 1976 WAS 5 PERCENT (WHICH MAY BE TOO LOW), THI WOULD STILL MEAN THAT ABSOLUTE LEVEL OF ECONOMIC ACTIVITY IN 1977 WOULD BE AS HIGH AS AT ANY OTHER TIME IN ITALY'S HISTORY (SEE TABLE 7). IN FACT, REAL GROWTH COULD FALL BY ALMOST 1.1 PERCENT IN 1977 AND STILL BE EQUAL TO 1974, WHICH WAS BEST YEAR OF PREVIOUS GROWTH CYCLE. FINALLY, EVEN IF REAL GROWTH WERE TO FALL BY AS MUCH AS 2.5 PERCENT, WHICH N EMBASSY OPINION IS OUTER LIMIT, 1977 GDP IN REAL TERMS WOULD BE ABOUT 2.4 PERCENT ABOVE THAT OF 1975. ADMITTEDLY, ZERO GROWTH IS CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 00569 04 OF 05 140914Z

NOT A DESIRABLE TARGET AND IT WOULD BE INTERPRETED NEGATIVELY BY MOST OF ITALY'S POLITICAL AND SONIAL FORCES, WITH ATTENDANT POLITICAL CONSEQUENCES FOR THE GOVERNMENT. ITALIAN ECONOMY WOULD BE CAPBLE OF BETTER PERFORMANCE WERE IT NOT FOR BALANCE OF PAYMENTS CONSTRAINT. HOWEVER, ZERO GROWTH IN 1977 WOULD BE WORTH THE EFFOT (THOUGH PERHAPS NOT RECOGNIZED AS SUCH) IF IT WERE RESULT OF STABILIZATION PROGRAM WHICH IMPROVED ITALY'S INFLATIONARY PERFORMANCE SUFFICIENTLY TO PERMIT GOOD EXPORT GROWTH AND A STRUCTURAL IMPROVEMENT IN INVESTMENT.

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 ROME 00569 05 OF 05 141054Z
ACTION EUR-08

INFO OCT-01 SS-14 ISO-00 FRB-01 NSC-05 NSCE-00 INR-05
CIAE-00 INRE-00 SP-02 L-01 EB-03 OMB-01 SSO-00 /041 W
-----141057Z 040592 /21
O 140845Z JAN 77
FM AMEMBASSY ROME

TO SECSTATE WASH DC IMMEDIATE 2158
TREAS DEPT WASH DC IMMEDIATE
INFO USMISSION EC BRUSSELS
USMISSION OECD PARIS

CONFIDENTIAL SECTION 5 OF 5 ROME 0569

LIMDIS

PASS FRB

20. TABLE 7 - GROWTH AND EMPLOYMENT 1974-1977 (BILLIONS
OF LIRE; PERCENT CHANGE)

	1974	1975	1976	1977E
GROWTH				
GDP (REAL TERMS)	67,053	64,545	67,772	67,772
PERCENT CHANGE	3.4	-3.7	5.0	-
EMPLOYMENT 1)				
(CHANGE IN 000'S)				
EMPLOYMENT	398	98	131	-150
UNEMPLOYMENT/				
UNDEREMPLOYMENT 2)	-88	238	10	100

E-EMBASSY ESTIMATE.

1) YEARLY AVERAGES OF ISTAT QUARTERLY SURVEYS (JANUARY,
APRIL, JULY, OCTOBER)

2) "UNDEREMPLOYMENT" IS SHORT-TIME WORK (LESS THAN 33
HOURS PER WEEK).

21. ITALIAN PRESS HAS ALSO BEEN FULL OF POLEMICS REGARDING
POSSIBLE INCREASE IN UNEMPLOYMENT IN 1977. MINISTER OF
CONFIDENTIAL

CONFIDENTIAL

PAGE 02 ROME 00569 05 OF 05 141054Z

INDUSTRY DONAT-CATTIN HAS CLAIMED THAT UNEMPLOYMENT
COULD RISE BY 600 THOUSAND. MINISTER OF LABOR ANSELMI
HAS REBUTTED ARGUMENT AS TOO PESSIMISTIC BUT SUGGESTED
FIGURE COULD REACH 200-300 THOUSAND. CERTAINLY,
600 THOUSAND FIGURE IS NOT CREDIBLE. EVEN 200-300 THOUSAND
INCREASE IN UNEMPLOYMENT, IN EMBASSY VIEW, SEEMS UNLIKELY.
DURING PREVIOUS BUSINESS CYCLE UNEMPLOYMENT PLUS UNDER-
EMPLOYMENT ROSE BETWEEN APRIL 1974 AND APRIL 1975
(ROUGHLY PEAK AND TROUGH OF UNEMPLOYMENT CYCLE) BY 434
THOUSAND. HOWEVER, LABOR SITUATION IN 1977 WILL BE
RATHER DIFFERENT. FIRST, AS NOTED ABOVE, ZERO GROWTH IN
1977 STILL WOULD RESULT IN CONTINUED LEVEL OF ECONOMIC
ACTIVITY WHICH WAS 5 PERCENT HIGHER THAN DURING 1975
RECESSION. SECOND, EMBASSY BELIEVES THAT SHAKE-OUT OF
LABOR FORCE DURING 1974-1976 CYCLE HAS ALREADY REDUCED
ANY EXCESS LABOR, SO THAT FURTHER REDUCTIONS IN 1977
WILL BE LESS LIKELY. THIRD, AS LAST BUSINESS CYCLE
SHOWED, IT IS EXTREMELY DIFFICULT IN ITALY TO LAY

OFF WORKERS. ALSO, TO EXTENT THAT WORKERS ARE PUT ON SHORT TIME, COMPENSATION IS SO HIGH AS TO NEARLY EQUAL FULL-TIME PAY. NONETHELESS, EMBASSY DOES ANTICIPATE SOME FURTHER INCREASE IN UNEMPLOYMENT AND UNDEREMPLOYMENT IN 1977, BUT OF MODEST AMOUNT. LIKELY HIGH-LEVEL/YOUTH COMPONENT OF INCREASED UNEMPLOYMENT COULD AGGRAVATE SOCIAL SITUATION BEYOND WHAT WERE NUMBER SUGGEST. ALSO, THERE COULD BE SOME REDUCTION IN SIZE OF LABOR FORCE REFLECTING WITHDRAWAL OF SOME DISCOURAGED WORKERS BECAUSE OF PERSISTENCE OF WEAK LABOR MARKET IN PAST TWO YEARS.

2. CONCLUSION. WHILE IT IS STILL TOO EARLY TO MAKE FINAL JUDGMENT, EMBASSY BELIEVES THAT GOI STABILIZATION PACKAGE WILL PROVE TO BE REASONABLE ADEQUATE. ANDREOTTI GOVERNMENT HAS DISPLAYED CONSIDRABLE TACTICAL SKILL AND FORTITUDE IN CONVINCING PUBLIC AND LABOR UNIONS OF SERIOUSNESS OF ECONOMIC PROBLEM AND HAS BEEN WILLING TO

CONFIDENTIAL

PAGE 03 ROME 00569 05 OF 05 141054Z

GO TO THE BRINK IN PRESSING FOR ADOPTION OF SERIOUS REMEDIES, AS IN THE CASE OF SCALA MOBILE. AT ONE POINT IT APPEARED THAT SUPPORT FROM DC MAJORITY IN CISL AND PCI MAJORITY IN CGIL WOULD PREVAIL IN OBTAINING RELUCTANT LABOR SUPPORT FOR SIGNIFICANT REVISION OF SCALA MOBILE MECHANISM. STRONG OPPOSITION BY PSI MINORITY IN CGIL AND PSI MAJORITY IN UIL IS LARGELY RESPONSIBLE FOR FAILURE OF THIS EFFORT AND HAS CAUSED PCI AND CGIL TO RETREAT IN FACE OF INTRANSIGENT POSITION TAKEN BY UIL WITH AMPLE LABOR GRASS ROOTS SUPPORT. GOI IS NOW FACED WITH MORE DIFFICULT TASK OF PUTTING TOGETHER HODGE-PODGE OF LABOR COST MEASURES WHICH WILL STILL BE BIG ENOUGH TO BE CONVINCING TO FOREIGN CREDITORS. WHILE THIS WILL NOT BE EASY, EMBASSY IS FAIRLY OPTIMISTIC THAT UNIONS CAN BE CONVINCED THAT THEIR OWN PORPOSALS FOR REDUCING LABOR COSTS ARE NOT SUFFICIENT TO LIMIT INFLATION, IMPOROVE INVESTMENT/ AND EMPLOYMENT PROSPECTS, OR SATISFY FOREIGN CREDITORS. MOREOVER, IT SHOULD NOT BE FORGOTTEN THAT UNION PROPOSALS INCLUDE MEASURES DESIGNED TO INCREASE PRODUCTIVITY (E.G., GREATER LABOR MOBILITY, REDUCED ABSENTEEISM, STAGGERED HOLIDAYS, ETC.) WHICH MAY NOT BE PARTICULARLY HELPFUL IN 1977 BUT WHICH COULD BE QUITE VALUABLE IN LONGER TERM IN RESTRAINING GROWTH OF ITALY'S UNIT LABOR COSTS. EMBASSY IS STILL SOMEWHAT CONCERNED ABOUT TREASURY DEFICIT PROBLEM. GOI IS TO BE COMMENDED FOR REVENUE MEASURES TAKEN TO DATE, AND TREASURY MINISTER STAMMATI HAS BEEN SURPRISINGLY FIRM IN DEFENDING 9,800 BILLION LIRE TARGET. THERE WILL CERTAINLY BE SOME ADDITIONAL TAX/MEASURES AND MANY OF POTENTIAL EXCESS EXPENDITURES CAN PROBABLE BE DEFFED. NONETHELESS, ADEQUACY OF REVENUE

IN 1977 IS STILL NOT ASSURED.

23. IN SUM, EMBASSY BELIEVES THAT FINAL STABILIZATION
PROGRAM WILL CERTAINLY MERIT MINIMUM IMF STANDBY OF SDR
450 MILLION, \$500 MILLION FROM EC (WHICH WILL ONLY
REPLACE PREVIOUS U.K. COMPONENT OF EC CREDIT), AND PERHAPS
CONFIDENTIAL

CONFIDENTIAL

PAGE 04 ROME 00569 05 OF 05 141054Z

SOME SHORT-TERM ASSISTANCE TO HELP BANK OF ITALY IRON
OUT TEMPORARY FLUCTUATIONS IN LIRA. WHETHER OR NOT
QUALITY OF PROGRAM WILL MERIT ADDITIONAL MEDIUM-TERM
ASSISTANCE IN FORM OF NEW CREDITS OR REFINANCING IS NOT
YET CLEAR. PRESUMABLE, TRANCHING OF IMF CREDIT AND
REGULAR REVIEWS OF PERFORMANCE UNDER NORMAL STANDBY
ARRANGEMENTS WILL OFFER OPPORTUNITY TO MONITOR SUCCESS
OF PROGRAM SO AS TO PROVIDE GUIDANCE ON JUSTIFICATION
FOR ANY ADDITIONAL FINANCIAL ASSISTANCE. VOLPE

CONFIDENTIAL

NNN

Message Attributes

Automatic Decaptoning: Z
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC STABILITY, ECONOMIC REPORTS, ECONOMIC PROGRAMS
Control Number: n/a
Copy: SINGLE
Sent Date: 14-Jan-1977 12:00:00 am
Decapton Date: 22 May 2009
Decapton Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977ROME00569
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D770014-0607
Format: TEL
From: ROME
Handling Restrictions:
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770151/aaaabsat.tel
Line Count: 731
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 943b71d9-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: CONFIDENTIAL
Original Handling Restrictions: LIMDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 14
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: LIMDIS
Reference: 76 ROME A-514, 76 ROME 20147, 76 ROME 19891, 76 ROME 19449, 76 ROME 18880
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 22-Nov-2004 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 3595855
Secure: OPEN
Status: NATIVE
Subject: CURRENT STATUS OF ECONOMIC STABILIZATION PROGRAM
TAGS: EFIN, IT
To: STATE TRSY
Type: TE
vdkvgwkey: odbc://SAS/SAS.dbo.SAS_Docs/943b71d9-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009